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1 UNITED STATES BANKRUPTCY COURT
2 SOUTHERN DISTRICT OF NEW YORK
3 Adv. Proc. No. 08-01789-smb (SIPA LIQUIDATION)
4 - - - - -
5 In the Matters of:
6 SECURITIES INVESTOR PROTECTION CORPORATION,
7 Plaintiff,
8 v.
9 BERNARD L. MADOFF INVESTMENT SECURITIES LLC,
0 Defendant.
1 - - - - -
2 BERNARD L. MADOFF,
3 Debtor.
4 - - - - -
5 United States Bankruptcy Court
6 One Bowling Green
7 New York, New York
8
9 February 25, 2015
20 10:03 AM
21
22
23 B E F O R E:
24 HON. STUART M. BERNSTEIN
25 U.S. BANKRUPTCY JUDGE

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2 08-01789-smb **Securities Investor Protection Corporation v.**

3 **Bernard L. Madoff Investment Securities**

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5 **HEARING re Trustee's Motion to Affirm Trustee's Determinations**

6 **Denying Claims of Claimants Holding Interests in S&P and P&S**

7 **Associates Partnerships**

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25 **Transcribed by: Lisa Beck**

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4 Substantively Consolidated SIPA Liquidation of
5 Bernard L. Madoff Investment Securities LLC and
6 the Estate of Bernard L. Madoff

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1 P R O C E E D I N G S

2 THE COURT: Please be seated. Madoff?

3 (Pause)

4 MS. VANDERWAL: Good morning, Your Honor.

5 THE COURT: Good morning.

6 MS. VANDERWAL: Amy Vanderwal, Baker Hostetler, on
7 behalf of the trustee.

8 THE COURT: Go ahead.

9 MS. VANDERWAL: We're here this morning on the
10 trustee's motion to affirm his determination of approximately
11 158 claims that relate to 36 objections. One objection was
12 received to the trustee's motion.

13 The claimants invested directly or indirectly with two
14 Florida partnerships, S&P Associates and P&S Associates. Both
15 partnerships had accounts with BLMIS in their names and they
16 were customers at BLMIS. The partnerships filed claims in
17 these proceedings; those claims were allowed. They had
18 received distributions and will continue to receive
19 distributions on the estate.

20 The trustee's denial over the objecting claimants'
21 claims because they are not customers under SIPA is consistent
22 with several prior decisions of this Court, the district court,
23 the Second Circuit in these proceedings as well as the Second
24 Circuit's decision in Morgan-Kennedy.

25 Several principles can be distilled from these

1 decisions that are applicable here today. First, SIPA should
2 be narrowly interpreted on the issue of who is a customer
3 because of the priority treatment granted to customers
4 thereunder. Second, purported customers have the burden of
5 demonstrating that they are deserving of the status thereunder.
6 Third, the critical aspect of the customer definition is the
7 entrusting of their cash or securities to the broker for the
8 purpose of trading securities. And finally and specifically,
9 claimants who did not hold accounts in their name with BLMIS,
10 who did not entrust their funds to BLMIS, who are not known to
11 BLMIS, who did not receive account statements and who are not
12 shown in the books and records of BLMIS are not customers.

13 Claimants here have failed to carry their burden to
14 demonstrate that they're customers and have provided no
15 evidence that gets around this well settled authority. Indeed,
16 in their responses that were provided to the discovery
17 propounded by the trustee, the claimants have conceded, among
18 other things, that they did not have accounts in their names at
19 BLMIS, they did not directly invest with or make withdrawals
20 from BLMIS and they did not interact with BLMIS.
21 Notwithstanding this, they make two principal arguments in
22 seeking their customer status. The first is that they owned
23 the funds that were invested at BLMIS and second is that they
24 exerted control over investment decisions made by the
25 partnerships. But both of these arguments fail.

1 First, the assertion that they had any ownership in
2 the funds that were invested with BLMIS is completely untrue.
3 The plain language of both the partnership agreement and
4 Florida partnership law provides that the funds that were
5 invested by the partnerships were owned by the partnerships.

6 THE COURT: But under prior law, they held the
7 partnership property as tenants in partnership, didn't they?
8 What does that mean?

9 MS. VANDERWAL: Well, that law was changed as of 1996.
10 And as of 1998, the current partnership law applies to all
11 partnerships (indiscernible).

12 THE COURT: So you think that if they had a property
13 right in those funds, a change in the law could deny them --
14 could it be they don't have property rights?

15 MS. VANDERWAL: First, I would --

16 THE COURT: Isn't that a violation of due process?

17 MS. VANDERWAL: I would first argue that even under
18 the prior law, it's questionable whether the level of rights in
19 the property rose to the level of ownership. But even if it
20 did, the due process that was built into the law was that there
21 was a two-year period before the law applied --

22 THE COURT: Yeah.

23 MS. VANDERWAL: -- to all partnerships --

24 THE COURT: But you know --

25 MS. VANDERWAL: -- that existed over --

1 THE COURT: -- if you look at the revised act, there's
2 a provision in the revised act which says this law applies to
3 partnerships and any repeal or amendment of this law applies to
4 partnerships. That's provision -- and that's to overcome, I
5 think (indiscernible) or some old Supreme Court case. The
6 Uniform Partnership Act didn't have the same provision.

7 MS. VANDERWAL: Well, our position that both the
8 partnership agreement and the law that is directly applicable
9 to the partnerships here clearly set out who owns the property.
10 For example, Section 602 -- or 601 -- sorry -- of the
11 partnership agreement clearly provides that the property is
12 owned by the partnership not the partners themselves.

13 So instead of actually owning the funds that are at
14 BLMIS, the claimants merely made contributions to the
15 partnership. They had an interest in the partnership. They
16 received profits from the partnership. And if they were to
17 withdraw from the partnership, they would receive the value of
18 their partnership interest. They didn't receive any particular
19 property back.

20 THE COURT: I thought some of the claimants were one
21 or more generations removed also. Were they --

22 MS. VANDERWAL: Some were indirect. Some were
23 indirect. They directed in the -- they invested in the trust
24 that invested in the partnership. So they were even farther
25 removed from a claim to this property that was invested with

1 BLMIS.

2 THE COURT: Do you know how much has been distributed
3 or what the net equity claim is of the two partnerships?

4 MS. VANDERWAL: I can tell you approximately that one
5 has an alleged claim of approximately two million and the other
6 was approximately 10 million. And so they have received the
7 distributions that all other customers have received to date.

8 THE COURT: Okay.

9 MS. VANDERWAL: So, in short, with respect to
10 ownership, the investors in feeder fund in the Second -- the
11 investors here are like the investors in the feeder fund in the
12 Second Circuit decision. They invested in an entity that
13 invested in Madoff. They themselves did not invest in Madoff.

14 With respect to the second argument that was put forth
15 by the claimants, they cannot demonstrate that they exerted
16 meaningful control over investment decisions. The provision of
17 the partnership agreement that they rely on merely provides
18 that majority consent is required to invest with the broker or
19 withdraw from a broker or grant that broker discretionary
20 investment power. So the control is limited, it's subject to
21 majority rule and it relates only to funds owned by the
22 partnership. Both this Court in the feeder fund decision and
23 the Second Circuit in Kruse have held that demonstrating some
24 level of control over investments or steering those investments
25 to BLMIS is not sufficient to establish customer status where

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1 there are no direct dealings with BLMIS and not that they're
2 not directly invested with BLMIS.

3 THE COURT: Is there any evidence in the case
4 that you're aware of that the relationship between the
5 partnerships and BLMIS or Madoff is disclosed to the partners
6 prior to Madoff's arrest? I saw the letter after Madoff's
7 arrest.

8 MS. VANDERWAL: Right. The papers submitted by the
9 claimants suggest that BLMIS was aware that the investors
10 were --

11 THE COURT: I'm asking if you're aware, for instance,
12 of offering memoranda or anything like that that said you're
13 investing -- the partnership is investing its fund with BLMIS.

14 MS. VANDERWAL: No. We haven't -- we requested
15 through discovery any information that would suggest that. We
16 haven't received that.

17 THE COURT: Okay. And Madoff isn't -- or BLMIS isn't
18 mentioned in the partnership agreement, is it?

19 MS. VANDERWAL: No.

20 THE COURT: Okay.

21 MS. VANDERWAL: In sum, we would just submit that the
22 claimants have failed to meet their burden to demonstrate that
23 these funds were entrusted -- these funds that were entrusted
24 to BLMIS were theirs and that they invested them for the
25 purpose of trading securities. So we would request that the

1 trustee's motion be granted.

2 THE COURT: Thank you.

3 MS. GORCHKOVA: Good morning, Your Honor.

4 THE COURT: Good morning.

5 MS. GORCHKOVA: Julie Gorchkova of Becker & Poliakoff
6 on behalf of the objecting claimants that were identified on
7 Exhibit A to Ms. Cheema's declaration in opposition to the
8 trustee's motion.

9 THE COURT: That's that 78 claimants, I believe?

10 MS. GORCHKOVA: Yes.

11 THE COURT: Okay. So are the other hundred -- and I'm
12 really asking is are the other half pro se in this? In other
13 words, they filed objections but they didn't respond to the
14 motion?

15 MS. GORCHKOVA: No. There was only one response
16 received to the motion.

17 THE COURT: Okay. But there are 158 --

18 MS. GORCHKOVA: Claims.

19 THE COURT: -- pro ses --

20 MS. GORCHKOVA: Some are pro se --

21 THE COURT: Okay.

22 MS. GORCHKOVA: Some are represented by other firms.
23 We didn't receive any other --

24 THE COURT: Okay. Go ahead.

25 MS. GORCHKOVA: Okay Our arguments are set forth in

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1 our opposition papers so I'm not going to rehash them here.
2 I'd like to instead focus primarily on addressing how the
3 customer opinions in the prior -- how the customer opinions in
4 this case are different from the facts that we have here. And
5 when I state the "customer opinions", what I'm referring to are
6 the earlier decisions involving the trustee's determination of
7 claims that are identified on pages 4 through 8 of the
8 trustee's motion papers and dealt with feeder fund investors
9 and pension plan participants both of which are very different
10 from the relationship that the partners had with BLMIS through
11 the partnerships in this case.

12 The partners in this case are readily distinguishable
13 from the claimants in the customer opinions in a very material
14 way. When examining the Morgan-Kennedy factors, unlike the
15 claimants in the customer opinions, the partners here have a
16 great deal of control over the actual money that was invested
17 through the partnerships. Indeed, the trustee admits at page 1
18 of his reply that although he categorizes conditional ability,
19 he nonetheless admits that the partners had an ability to --
20 had an ability to vote on limited issues relating to how the
21 partnership as a whole would make investments. The partners --

22 THE COURT: Is there any evidence that that occurred
23 in this case with S&P or P&S? In other words, we know about
24 the 51 percent majority provision. Was there any evidence that
25 the partners acting as a majority, they were selected or fired

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1 a broker or armed the broker with discretionary trading powers?

2 MS. GORCHKOVA: No. BLMIS -- to my knowledge, BLMIS
3 was the only entity into which the partnerships invested from
4 the --

5 THE COURT: Well, there was --

6 MS. GORCHKOVA: -- start of the partnerships.

7 THE COURT: They signed -- I know they signed the
8 trading agreements about two weeks after the partnership
9 agreements were signed.

10 MS. GORCHKOVA: I'm sorry?

11 THE COURT: The trading agreements were signed about
12 two weeks after the partnership agreement was signed.

13 MS. GORCHKOVA: Correct. And at all times, the
14 partnerships were invested with BLMIS.

15 THE COURT: But supposedly, at quarterly meetings, the
16 partners were supposed to review the partnerships'
17 relationships with brokers. Is there any evidence in minutes
18 or anything like that that they ever reviewed a relationship
19 with BLMIS?

20 MS. GORCHKOVA: I have not seen any minutes submitted
21 from our clients. But I know that under the partnership
22 agreement and based on knowledge that I obtained while having
23 discussions with the partners --

24 THE COURT: That sounds like hearsay.

25 MS. GORCHKOVA: Right. Nonetheless, I think the

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1 important thing is that it was the ability -- they had the
2 ability to do that irrespective of whether it was done or not.

3 THE COURT: A majority of the partners had that legal
4 ability, I would agree.

5 MS. GORCHKOVA: And while the trustee characterizes
6 this as a very limited level of control, we disagree. And we
7 think that in a situation where you have a collective
8 investment, that may perhaps be the greatest level of control
9 that an investor can have --

10 THE COURT: What do you mean by a collective
11 investment?

12 MS. GORCHKOVA: Well, for example, under the
13 partnership agreement, only 51 percent of the partnership -- of
14 the interest were required to either change the investments or
15 maintain the investments. For instance, if the partnership
16 agreements require that a 95 percent approval or a 75 percent
17 approval be required, that would be less control than --

18 THE COURT: What about 60 percent?

19 MS. GORCHKOVA: Sixty percent would be less control
20 than 51 percent.

21 THE COURT: What if it said 40 percent?

22 MS. GORCHKOVA: Forty percent would be greater but it
23 would not be the majority.

24 THE COURT: But 51 is much more in control, right?

25 MS. GORCHKOVA: Fifty-one is greater control when you

Page 15

1 look -- yes. Fifty-one is the greatest amount of control that
2 you can have when looking at the majority of the partners.

3 THE COURT: Okay.

4 MS. GORCHKOVA: Section 804 of the partnership
5 agreement provided for quarterly meetings --

6 THE COURT: Right.

7 MS. GORCHKOVA: -- as Your Honor acknowledged. And at
8 the quarterly meetings, the partners were given an opportunity
9 to evaluate whether investment would be maintained with BLMIS
10 or if it would be transferred somewhere else.

11 THE COURT: Is there any evidence that they even knew
12 that BLMIS was the partnerships' broker?

13 MS. GORCHKOVA: Yes.

14 THE COURT: What's the evidence?

15 MS. GORCHKOVA: Our answers to requests for
16 admissions.

17 THE COURT: But that's not evidence. Ms. Chaitman
18 signed that. Is she going to testify as to what the general
19 partners told the managing partners or the managing partners
20 told BLMIS? She can't testify to that. That's not evidence.

21 MS. GORCHKOVA: Ms. Chaitman cannot testify to that.
22 And although you are right that the requests for admissions
23 were signed by Ms. Chaitman only, under the Federal Rules of
24 Civil Procedure, they only need to be signed by -- they can be
25 signed by either Ms. Chaitman or --

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1 THE COURT: I understand that but that avoids the
2 effect of a deemed admission. But the answers are not
3 evidence, are they?

4 MS. GORCHKOVA: Umm --

5 THE COURT: How can Ms. Chaitman --

6 MS. GORCHKOVA: They're not. But --

7 THE COURT: It would be like her giving an affidavit
8 as to the --

9 MS. GORCHKOVA: But if it's --

10 THE COURT: You are not deemed to admit whatever it is
11 the response was. But the response itself is not evidence, is
12 it?

13 MS. GORCHKOVA: Perhaps not but then the trustee -- if
14 that's -- if Your Honor recognizes that that's a factual issue
15 then the trustee can go forward and take discovery.

16 THE COURT: How can there be a factual issue without
17 any evidence to raise a factual (indiscernible)?

18 MS. GORCHKOVA: We think that there is -- that the
19 answers themselves would be sufficient.

20 THE COURT: Okay. Go ahead.

21 MS. GORCHKOVA: Furthermore, if it turned out that one
22 of the partners wanted to conduct a vote as to whether the
23 investment would be invested somewhere else or maintained with
24 BLMIS and he was not happy with the result, he also had -- he
25 or she had an opportunity to withdraw from the partnership

1 within 30 days notice.

2 THE COURT: That's true about the feeder fund case,
3 though.

4 MS. GORCHKOVA: Yes. But the feeder fund cases are
5 very distinguishable from the situation that we have here.

6 THE COURT: But not on the right to withdraw that you
7 just mentioned. Sure, they had a right to withdraw their money
8 from the partnership, right?

9 MS. GORCHKOVA: Perhaps in that aspect alone. But
10 here, we don't just have the right to withdraw. We have the
11 right to withdraw if they're not satisfied with the vote that
12 happened every three months.

13 THE COURT: Well, they can withdraw for any reason or
14 no reason, right?

15 MS. GORCHKOVA: And -- yes.

16 THE COURT: Okay.

17 MS. GORCHKOVA: The level of control that the partners
18 had here is very different and more direct than the level of
19 control that was present in the feeder fund decisions. In the
20 first feeder fund decision, the Second Circuit looked at
21 investors who invested into two entities that then invested
22 into hedge funds which then invested with BLMIS. And there, in
23 determining whether the claimants or investors satisfied
24 customer status, one of the things that the Court emphasized
25 was the level of control that the investors had over the feeder

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1 funds' decisions to invest. And there, the Court concluded
2 that based on its review of various feeder fund materials, such
3 as the private placement memoranda, that the investors yielded
4 all of their control to the feeder funds. That is very
5 different from the situation that we have here. And if we look
6 at the private placement memorandum that the Second Circuit
7 actually cited -- that quoted in the decision there, the
8 private placement memorandum stated that the general partner,
9 not the investors, had the sole right to hire and terminate
10 investment advisors. That's precisely the opposite of the
11 situation that we have here in the partnerships agreement.

12 Now the trustee, in his reply, takes the position that
13 whether the partners retained complete control over the
14 decision regarding the investment as immaterial in light of
15 some of the language in the Second Circuit decision. And he
16 cites -- in his reply papers, he stated "The Second Circuit
17 held in Kruse -- which is the feeder fund decision that I was
18 talking about -- that 'even if appellants could demonstrate
19 that they exercised some level of control over the Feeder
20 Funds' investments, that fact, standing alone, would be
21 insufficient.'"

22 THE COURT: What else did they say? There's more to
23 that --

24 MS. GORCHKOVA: He cites --

25 THE COURT: There's more to that. No.

1 MS. GORCHKOVA: Yes.

2 THE COURT: There's more to that quote.

3 MS. GORCHKOVA: -- "would be insufficient to confer
4 'customer' status on appellants given that, individually, they
5 'made no purchases, transacted no business, and had no dealings
6 whatsoever' with BLMIS."

7 THE COURT: Isn't that what occurred here?

8 MS. GORCHKOVA: No. First, we would submit that that
9 portion of the Second Circuit decision is not a holding
10 contrary to what the trustee asserted but it's --

11 THE COURT: But the Second Circuit was quoting more
12 than Kennedy. Wasn't that the holding of Morgan-Kennedy.

13 MS. GORCHKOVA: No, not to my knowledge.

14 THE COURT: That's a quote from Morgan-Kennedy that
15 the Second Circuit is quoting in Kruse.

16 MS. GORCHKOVA: Yes, starting from "'made no
17 purchases, transacted no business, and had no dealings
18 whatsoever' with BLMIS" is a quote from Morgan-Kennedy. But
19 when the Second Circuit made that statement, it was made in the
20 context of -- it actually says the appellants. And the
21 appellants in that case were feeder fund investors which our
22 position is that there are significant -- materially different
23 in a different position than our clients are. And in addition
24 to the fact that we think that that portion is dicta, there's
25 nothing in that decision -- in the Second Circuit decision that

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1 would suggest that that would apply to here, that the same
2 statement would be applied in a different context outside of
3 feeder funds.

4 Moreover, I don't think it's appropriate to speculate
5 at this point what some level of control the Second Circuit
6 would be referring to.

7 THE COURT: All right. But can I ask you a slightly
8 different question? Assuming that they had some control but
9 they never exercised it or there's no evidence that they ever
10 exercised it, would that be relevant?

11 MS. GORCHKOVA: I don't believe so. I think that the
12 Court needs to look at the governing documents just like the
13 Second Circuit looked at the private placement memorandum in
14 the feeder fund case. And if the partners had the authority to
15 exercise a control then that's what the Court should look at as
16 opposed to looking at whether there was an actual exercise of
17 control.

18 The trustee also cites to the -- relies heavily on the
19 district court's decision in SIPC v. Jacqueline Green Rollover
20 Account which, as Your Honor probably -- is the ERISA
21 account -- is the ERISA decision and this Court's recent
22 decision in connection with the trustee's motion relating to
23 his denial of claims of other plan participants including the
24 Daprex claimants. And he cites those two decisions to argue
25 that the claimants in those cases had a greater deal of control

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1 than the customers -- than the partners have here. And I would
2 submit two things. First, the ERISA decision was limited
3 solely to the issue of how ERISA affects, if at all, the
4 determination of customer status of ERISA plan participants.
5 And although the Court did look at the Morgan-Kennedy factors,
6 it evaluated those factors in the context of -- in numerous
7 contexts in terms of whether a certain argument that was made
8 based on ERISA would somehow impact how one or more factors
9 would be decided. And in fact, in the ERISA decision, the
10 Court specifically said that individual factual issues such as,
11 for instance, some claimants submitted additional evidence
12 showing that they actually had contact with BLMIS or that they
13 made payments directly to BLMIS, the Court declined to consider
14 that. The Court said that those issues that are not related to
15 ERISA specifically is not before the Court and that the
16 bankruptcy court at a later time can determine those individual
17 issues. So the level of control there was not before the
18 Court.

19 Similarly, with respect to the Daprex decision, I
20 believe that the control that the partners have here is
21 significantly more than the claimants had in the Daprex
22 decision. There, you had participants in pension -- in
23 employee pension plans and, yes, although the participants had
24 the ability to withdraw or invest or rollover their money, they
25 did not have the authority as a whole to control how the money

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1 of the actual plan was invested whereas here, the partners did.
2 Although it was a collective effort, nonetheless that control
3 was there.

4 And just in terms of some of the other factors that
5 Morgan-Kennedy looks at, as stated in our answers to requests
6 for admissions, the partners that the partnership itself was
7 investing with BLMIS and the partnerships' managing partner,
8 Mr. Sullivan, in fact, told BLMIS that this money was being
9 invested on behalf of partnerships.

10 THE COURT: So what? So what if they knew that --
11 I'll grant you that BLMIS knew that these were general
12 partnerships and therefore would know that the investments
13 probably came from the capital contributions of the partners.
14 But what does that mean?

15 MS. GORCHKOVA: Well, I think it --

16 THE COURT: Why is that legally significant?

17 MS. GORCHKOVA: I think it's just another factor that
18 supports a finding of customer status in this particular case.
19 Perhaps not alone, but in Morgan-Kennedy, the Court looked at
20 whether the plan participants were anonymous and not --

21 THE COURT: Well, weren't they anonymous here? Is
22 there any -- are there any BLMIS records that identify any of
23 these partners?

24 MS. GORCHKOVA: Not to my knowledge.

25 THE COURT: So they were anonymous to BLMIS even if

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1 BLMIS knew that they were partners who were investing in the
2 two Florida partnerships that in turn were investing in BLMIS.

3 MS. GORCHKOVA: Perhaps the identity, the actual
4 identities of the partners, yes. But I think that given that
5 this is a partnership that collectively invested funds, there's
6 also a different level of expectations that the partners have
7 in being deemed customers given --

8 THE COURT: But can I -- you know, all of these feeder
9 fund -- or most of the feeder fund cases involve limited
10 partnership feeder funds. Isn't the same true with those
11 cases, that BLMIS should have known that they're partnerships
12 and therefore the funds are coming from the contributions of
13 partners?

14 MS. GORCHKOVA: Perhaps but my point is that in this
15 particular situation where you have partners that retain the
16 control to make the investment decisions that there's a greater
17 expectation for them, that they would be recognized as
18 customers given the fact that they had this control which is
19 distinguishable from the feeder fund cases.

20 THE COURT: Okay. I got it.

21 MS. GORCHKOVA: And one other fact that I would just
22 like to address. Although the Florida Partnership Act was
23 amended in 1998 and it no longer provides that the co-ownership
24 of property -- that the partnership properties co-owned by the
25 partners, the reason why we cited it is because I think it's

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1 important because it demonstrates the expectation of the
2 partners when the partnership was formed.

3 THE COURT: Do you take the position that the new law
4 repealed whatever rights were -- property rights were granted
5 to the partners under the old law? In other words, the trustee
6 is arguing that the old law was repealed and whatever it gave
7 you, you no longer have.

8 MS. GORCHKOVA: Not necessarily. I think that the
9 partners would be able to opt out of it. I don't know --

10 THE COURT: Opt out of the new law?

11 MS. GORCHKOVA: I think they -- because partnership
12 law is generally governed by contract law.

13 THE COURT: Okay. So you're saying that they could
14 opt out of it through the partnership agreement.

15 MS. GORCHKOVA: I believe so.

16 THE COURT: And what does the partnership agreement
17 say in this case?

18 MS. GORCHKOVA: To my knowledge, it was not amended in
19 light of the change in the law.

20 THE COURT: But what does the partnership agreement
21 say about the ownership of the property or the individual
22 partner's rights in the property?

23 MS. GORCHKOVA: The partnership agreement does not
24 talk about the co-ownership of the property, whether --

25 THE COURT: Sure. Doesn't it say that the partners

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1 can't seek to partake in the property?

2 MS. GORCHKOVA: Yes.

3 THE COURT: Okay.

4 MS. GORCHKOVA: But the partnership agreement also
5 says that upon termination that the partnership assets will be
6 distributed in accordance with the partnership shares. And our
7 position would be --

8 THE COURT: But every partnership agreement says that.

9 What do you think is going to happen on dissolution or
10 termination? The debts are paid and then the equity is paid
11 out.

12 MS. GORCHKOVA: One other point that I'd just like to
13 address is the issue raised by the trustee with respect to our
14 answers to the requests for admissions and that they should not
15 be considered by the Court. The trustee cites Rule 33 in
16 response saying that requests for admissions under Rule 33 have
17 to be sworn.

18 THE COURT: Under Rule 36.

19 MS. GORCHKOVA: Right. It's Rule 36 -- right. That
20 applies. But under Rule 36, they don't have to be sworn.

21 THE COURT: I understand. I don't have a problem with
22 how the responses -- with the responses. The fact that they
23 were signed by Ms. Chaitman and that isn't a deemed admission
24 of whatever that particular request was. But that's a
25 different issue from saying that the responder can use the

1 admissions -- really the denials -- as evidence.

2 MS. GORCHKOVA: Thank you.

3 THE COURT: Okay. Anything else? SIPC. I think we
4 should have (indiscernible) for the opposition but go ahead.

5 MR. KELLEY: Your Honor, Nathanael Kelley for SIPC.

6 I believe the trustee's counsel has stated the case
7 very clearly and I don't want to repeat what has been said
8 there. And I'll give her the opportunity to respond but I just
9 wanted to offer SIPC --

10 THE COURT: Your support?

11 MR. KELLEY: -- support and see if you had any
12 questions.

13 THE COURT: I have no questions. Thank you.

14 MR. KELLEY: Thank you, Your Honor.

15 MS. VANDERWAL: Your Honor, just very briefly. As I
16 mentioned earlier, the six (indiscernible) decisions on four of
17 the trustee's motions as well as Morgan-Kennedy are directly
18 relevant here. In each case, there were separate legal
19 entities in which people invested that, in turn, invested in
20 BLMIS.

21 In terms of control, as Your Honor recognized, no
22 evidence has been submitted to this Court in terms of exercise
23 of control, in terms of conversations between managing partners
24 and BLMIS. None of that -- there is no evidence of that before
25 the Court at this time. And the other thing --

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1 THE COURT: Suppose there was that evidence in this
2 case, would it then be the trustee's position that they're
3 customers?

4 MS. VANDERWAL: If they -- just because BLMIS or there
5 were other people who had invested?

6 THE COURT: Let's say we got an affidavit from
7 somebody who said, you know, I told -- the managing partner
8 told me that this money was going to be invested through the
9 partnership with BLMIS and that's why I did it.

10 MS. VANDERWAL: And our position is that that would
11 not be sufficient --

12 THE COURT: Why not?

13 MS. VANDERWAL: -- because it doesn't satisfy the most
14 essential factor that has been identified from this body of
15 case law which is that the purported customer owned the funds
16 that are invested with BLMIS.

17 THE COURT: All right. Thank you.

18 MS. VANDERWAL: Thank you.

19 THE COURT: S&P Associates and P&S Associates,
20 collectively "the Partnerships", are Florida general
21 partnerships that had accounts with BLMIS and essentially acted
22 as feeder funds investing all of their partnership funds with
23 BLMIS. This motion concerns the customer status of the general
24 partners of the partnerships. They never invested directly
25 with BLMIS. Instead, they invested directly with the

1 partnerships or indirectly with entities that became general
2 partners of the partnerships and invested their own funds
3 through the partnerships.

4 For the sake of convenience, I will refer to anyone on
5 invested directly or indirectly with the partnerships as
6 partners.

7 Except as noted, the facts are not in dispute and are
8 derived from the declarations of Bik, BIK, Cheema, C-H-E-E-M-A,
9 and Vineet, V-I-N-E-E-T, Sehgal, SEHGAL, submitted on this
10 motion and the documents attached to those declarations. The
11 partnerships were formed in 1992 and were governed by nearly
12 identical partnership agreements. Their purpose was to invest
13 in all types of market-placed securities, Partnership
14 Agreements, Section 2.02, and were funded with initial capital
15 contributions by the partners. Partnership Agreements, Section
16 4.01. Michael D. Sullivan and Greg Powell served as the
17 managing general partners and had the exclusive authority to
18 manage and control the day-to-day operations of the partnership
19 and maintain the partnership property. Partnership Agreements,
20 Section 8.01. Nevertheless, the general partners could have a
21 say in the selection of brokers. For example, a majority of
22 the partners in interest could cause the partnership to
23 terminate or allow a specific broker selected by the majority
24 and grant their selected broker discretionary investment powers
25 with the partnerships' investment funds. Partnership

1 Agreement, Section 2.02.

2 In addition, the partnership agreements at Section
3 8.04 stated that the partners would review any broker's
4 engagement with the partnership at the regular quarterly
5 meetings.

6 As noted, the partnerships maintained accounts with
7 BLMIS and following the commencement of the SIPA liquidation,
8 filed customer claims with the trustee based on their alleged
9 account statements dated November 30, 2008. According to the
10 trustee, the partnerships' claims have been allowed in an
11 amended amount. Each has received either payment of or the
12 benefit of a 500,000 dollar SIPC advance and interim
13 distributions have been made to each of them from the customer
14 fund maintained by the trustee.

15 Numerous partners also filed their own customer
16 claims. The trustee disallowed those claims on the basis that
17 the partners were not customers of BLMIS within the meaning of
18 SIPA. One hundred fifty-eight partners objected to his claim
19 determinations and this motion seeks to affirm his disallowance
20 of the partners' claims. The motion elicited the response from
21 78 partners represented by the law firm, Becker and Poliakoff
22 LLP. Although approximately 50 percent of the objecting
23 partners did not respond to the motion, I will refer to the
24 entire group as the objecting partners.

25 In SIPC v. BLMIS, 515 B.R. 161 (Bankr. S.D.N.Y. 2014),

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1 the Court reviewed the decisions by this Court, the district
2 court and the Second Circuit relating to the customer status of
3 persons who did not have accounts with BLMIS and instead
4 invested with entities that, in turn, invested directly with
5 BLMIS. To summarize briefly, customer status under SIPA is
6 narrowly interpreted. The "critical aspect" of the customer
7 definition is "the entrustment of cash or securities to the
8 broker-dealer for the purposes of trading securities". The
9 indicia of customer status include a direct financial
10 relationship with BLMIS, a property interest in the funds
11 invested directly with BLMIS, securities accounts with BLMIS,
12 control over the account holders' investments with BLMIS and
13 identification of the alleged customer in BLMIS' books and
14 records. Finally, the claimant has the burden of showing that
15 he or she is a customer, *id.* at page 165-68.

16 The objecting partners have failed to sustain their
17 burden of proof. They did not entrust any cash or securities
18 with BLMIS. They invested with the partnerships who, in turn,
19 invested with BLMIS. They have no direct financial
20 relationship with BLMIS. They did not deposit money with or
21 withdraw money from BLMIS or receive investment statements or
22 tax statements in their own names from BLMIS. The documents
23 produced by the trustee show that all communications with or by
24 the partnerships went through Sullivan or Powell and all
25 deposits and withdrawals were made by them in the names of the

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1 partnerships. Thus, even if BLMIS knew or surmised that the
2 partnerships' BLMIS accounts were funded with partners'
3 contributions, there is no evidence that BLMIS maintained
4 records identifying the partners or even knew who they were,
5 and the fact remains that the partners did not entrust anything
6 to BLMIS.

7 The objecting partners nevertheless contend that the
8 controlling decisions including Kruse v. Bricklayers and
9 Bricklayers and Allied Craftsman Local 2 Annuity Fund, (In re
10 BLMIS), 708 F.3d 422 (2nd Cir. 2013), and SIPC v. Morgan,
11 Kennedy and Co., 533 F.2d 1314 (2nd Cir.), cert. denied. 426
12 U.S. 936 (1976), are distinguishable for three reasons. First,
13 the partners had a specific interest under Florida law in all
14 partnership property invested with BLMIS. Second, BLMIS knew
15 that each partner had made a decision to entrust his or her
16 funds with BLMIS. Third, the partners had the ability to
17 control the investment decisions because they had the authority
18 to allow or terminate a specific broker and allow a broker to
19 have discretionary investment powers with the partnerships'
20 funds.

21 The partners had no interest in the property at the
22 partnerships under current Florida law. Florida Revised
23 Uniform Partnership Act ("Florida revised UPA") declares that a
24 partnership is a legal entity distinct from its partners.
25 Florida statute Section 620.8201(1). "Property acquired by a

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1 partnership is property of the partnership and not of the
2 partners individually," id. Section 620.8203, and "Partnership
3 property is owned by the partnership as an entity not by the
4 partners as co-owners", id. Section 620.8501.

5 In addition, the partnership agreements provide that
6 all property acquired by the partnerships would be owned by and
7 in the name of the partnership and each partner expressly
8 waived his right to require the partition of any partnership
9 property. Partnership Agreement, Section 6.01.

10 The objecting partners did not dispute the current
11 state of the law or the text of the partnership agreements.
12 Instead, they argue that the partnerships were organized in
13 1992 under the former Florida Uniform Partnership Act ("Florida
14 UPA") and Section 620.675 of that law provided, among other
15 things, that "at the inception of an incident to the
16 partnership relationship, each partner acquires certain
17 property rights [including] his rights in specific partnership
18 property."

19 The Florida UPA was repealed by the Florida Revised
20 UPA, effective January 1, 1998, see 6 - Part 1 U.L.A. 24
21 (2001), but the objecting partners imply that the repeal did
22 not affect the rights granted under the repealed law. Assuming
23 the former law governed the partners' rights, they still had no
24 right to the funds in the partnerships' BLMIS accounts. Former
25 Florida statute Section 620.68 provided that subject to the

1 Florida UPA and the partnership agreement, a partner could not
2 possess specific partnership property for non-partnership
3 purposes absent the consent of all partners. There is no
4 evidence of such consent here. But even if there was, it would
5 be irrelevant. The partnership agreements provided, as noted,
6 that the partners had no right to the partnership property and
7 waived their right to partition. Accordingly, the partner had
8 no right to possess the partnerships' BLMIS investments under
9 the prior law and certainly has no right in the specific
10 partnership property under the current law.

11 Next, the objecting partners offered no admissible
12 evidence to support their contention that BLMIS knew that they
13 had invested with the partnerships because they wanted to
14 invest with BLMIS. Instead, the objecting partners cite to
15 their responses to the trustee's request for admissions. The
16 responses were signed by Helen Chaitman, Esquire, the attorney
17 for the objecting partners. And the relevant response consists
18 of multiple hearsay. It is offered to prove that the objecting
19 partners told the managing partners who told BLMIS that the
20 objecting partners were investing in the partnerships in order
21 to invest in BLMIS. It is noteworthy that no objecting partner
22 offered an affidavit to that effect that he told the managing
23 general partners that he was investing in the partnerships in
24 order to invest in BLMIS. Nor did the objecting partners
25 submit an affidavit from either of the managing general

1 partners attesting to what they told representatives of BLMIS.

2 Furthermore, the partnership agreements did not
3 mention Madoff, a significant omission given that the
4 partnership agreements were dated December 11, 1992 and that
5 BLMIS trading agreements were dated December 28, 1992. Thus,
6 the partnerships with BLMIS investors from the onset. Nor is
7 there any documentary evidence in the form of offering
8 memoranda or partnership meeting minutes indicating that the
9 partnerships solicited partners with a promise to invest in
10 BLMIS, reviewed and/or approved BLMIS as a broker, invested
11 BLMIS with discretionary trading authority or that the
12 partnership ever informed the partners of its relationship with
13 Madoff or BLMIS until Madoff's arrest. In fact, when Sullivan
14 informed the P&S partners that Madoff had been arrested and all
15 of the partnerships' funds had been invested with BLMIS, his
16 letter did not suggest that the partners already knew that the
17 partnership was invested with BLMIS.

18 But even if the objecting partners or some of them
19 sought to invest in the partnerships in order to invest
20 indirectly with BLMIS, they still would not be customers. They
21 entrusted their money to the partnerships not BLMIS and they
22 dealt with the partnerships not BLMIS. However, the
23 partnerships hold allowed customer claims and received
24 distributions. The partners have the right under Florida's
25 partnership laws and the partnership agreements to look to the

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1 partnerships to recover at least some of their losses.

2 Lastly, although the partnership agreements authorized
3 the majority of the partners to direct the partnerships to
4 select or terminate a particular broker or arm a broker with
5 the discretionary trading authority, there is no evidence that
6 this ever occurred. Moreover, the right belonged to 51 percent
7 of the partners acting as a majority and did not empower any
8 individual to dictate an investment, select the broker or
9 withdraw money from BLMIS. As an individual, the partner could
10 only withdraw his investment from the partnership. He had no
11 right or ability to control his "share" of the partnerships'
12 investments with BLMIS.

13 But even if the partners had some level of control
14 over the partnerships' investments, "that fact, standing alone,
15 would be insufficient to confer 'customer' status on appellants
16 [the partners] given that, individually, they 'made no
17 purchases, transacted no business, and had no dealings
18 whatsoever' with BLMIS." Kruse, 708 F.3d at 427 (quoting
19 Morgan, Kennedy, 533 F.2d at 1318).

20 Accordingly, the objecting partners have failed to
21 sustain their burden of proving that they are SIPA customers of
22 BLMIS. The Court has considered the objecting partners
23 remaining arguments and concludes that they lack merit. Settle
24 order on notice to counsel to the objecting partners and to the
25 objecting partners that appeared pro se.

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1 Thank you.

2 MS. VANDERWAL: Thank you, Your Honor.

3 (Whereupon these proceedings were concluded at 10:47 a.m.)

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2 I N D E X

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4 R U L I N G S

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7	determination denying claims of claimants		
8	holding interests in S&P and P&S Associates		
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2 C E R T I F I C A T I O N

3

4 I, Lisa Beck, certify that the foregoing transcript is a true
5 and accurate record of the proceedings.

6

7 
Lisa Beck

Digitally signed by Lisa Beck
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email=digital1@veritext.com,
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Lisa Beck (CET**D 486)

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AAERT Certified Electronic Transcriber

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Date: February 26, 2015

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[& - approval]

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